

Poverty Reduction Strategy (PRS) Implementation Forum
16 November 2005
Session: 3

**Enhancing Competitiveness and Promoting Trade, Investment and
Private Sector Development in Bangladesh**

**[Paper presented by Mahmudur Rahman, Advisor: Energy & Mineral Resource
Division and Executive Chairman, BOI, Bangladesh]**

Comments by Dr. Salehuddin Ahmed: Governor, Bangladesh Bank

Mr. Chairman,
Honourable Advisor and Chairman BOI: Mr. Mahmudur Rahman
Distinguished participants
Ladies and Gentlemen

I am delighted to be here. It is indeed a great pleasure to be able to discuss on an important paper by Mr. Mahmudur Rahman on: "*Enhancing Competitiveness and Promoting Trade, Investment and Private Sector Development in Bangladesh*" considered a center piece of the newly launched PRSP. Mr. Rahman is eminently suitable to talk about the issue from the vantage point of view of being the dynamic head of the BOI responsible for facilitating private investment in the country.

Main Points and Issues Highlighted in the Paper

- ❖ The paper rightly notes that private investment and more particularly FDI is not only rising but also picked up sharply in recent years reflecting strengthening of macroeconomic stability, as well as improvements in some elements of competitiveness and investment climate. As a matter of fact I would say published BBS data underestimate the increase in investment-GDP ratio that has occurred in recent years owing mainly to inadequate coverage. Detailed data on imports of construction materials and capital goods clearly indicate sharp increase in private investment in recent years in such sectors as textiles and RMG (as part of the restructuring of the industry), telecom, pharmaceuticals, banking and other services
- ❖ The paper also correctly notes, export led robust growth of manufacturing production and employment, substantial trade liberalization during the last decade or so as well as recent reform initiatives to reduce cost of doing business and improvement in competitiveness. I agree with the author that the main challenge lies in the areas of improving infrastructure, human resources, regulatory environment and capacity building while reducing corruption and improving governance. These issues have also come up in a number of surveys as critical constraints for improving business climate. While some initiatives have been taken to address the constraints, lot more needs to be done to give a boost to private sector led development highlighted in the paper and the recently formulated PRS.

I know that PRS have also identified a number of critical areas noted above as essential elements to further improve business climate. We all agree that the challenge lies in implementing these. To attract FDI BOI in recent times has done a commendable job in addressing some regulatory barriers and enhancing inter-agency coordination. Let me elaborate one or two areas where central bank is also playing a major role, that of expanding the access and reducing the cost of finance.

Addressing Infrastructure Bottlenecks—Critical Constraint to Growth

- ❖ Recognizing the critical role infrastructure, (notably power, telecom, ports and roads) plays in improving the competitiveness and business climate in the country, in late August *Bangladesh Bank and the BOI in collaboration with the World Bank organized an international workshop on Infrastructure Financing in Bangladesh*. It brought together a number of international and national experts to brainstorm operational and policy issues relating to promotion of **public-private partnership** in infrastructure development, drawing on international best practices.
- ❖ **Findings of the workshop** indicate that the presence of various risks and uncertainty relating mainly to policy/regulatory issues hinder private participation in infrastructure. These and lack of long-term funds also explain reluctance of financial institutions to finance infrastructure projects. Workshop a host of debt, equity and other financial market instruments that can be used to finance long-term infrastructure projects and mitigate/transfer various kinds of risks. **In line with the recommendations of the workshop** and based on our experience, we are putting in place a refinancing facility with support from the World Bank to facilitate long-term funding for infrastructure. While government is doing its part by creating PICOM, Telecom and Energy Regulatory Commissions and should do more, at the same time private sector and financial institutions must also come forward with new projects.

Improving Governance in Financial Sector

Improvements in governance and regulations have also been identified as a critical step for improving business climate. In this regard PRSP Policy Matrix identifies detailed Targets and Actions in these areas.

- ❖ Let me take this opportunity to summarize the steps that have been taken in recent years to improve governance and regulation in the financial sector. For the Private Commercial Banks, Bangladesh Bank has (i) raised the minimum capital requirement to Tk. 1 billion (from Tk. 200 million) or 9 percent (from 8 percent) of the risk-weighted assets; (ii) reduced the single party exposure limit to 25 percent of the bank's capital; enforced stricter policy of loan provisioning and write-off and permitted dividend declaration by banks in excess of 20 percent only if equivalent amount is put off as reserves; (iii) reduced the number of directors on bank boards and raised the qualifications for board membership; (iv) revamped the

money loan courts to make them more effective; (v) made possible effective use of credit information bureau. For NCBs, BB has signed MOU with them limiting their operations and credit growth; introducing private management in one bank while bringing in external advisors for the other three.

As a result overall health of the banking system improved markedly in recent years. The share of PCBs in total assets exceeded for the time that of NCBs. Gross and net NPL ratios declined to single digit level for PCBs and substantially for NCBs. Profitability has risen for PCBs and real interest rates have shown a declining trend with the reduction in the spread between the deposit and lending rates. This led to rapid growth in private sector credit during the last 2 years or so.

However, as noted in the PRSP document much more remains to be done to create a competitive and efficient banking system capable of meeting the demand of financial services at a competitive interest rate.

- ❖ First, macroeconomic financial stability must be maintained in the face adverse external and domestic shocks and growing demand on public resources.
- ❖ Second, speedy implementation of the reform of the NCBs and the financial sector development programme will be critical in supporting private sector led investment and growth.
- ❖ Our future priorities include further improving efficiency of the financial system, developing financial markets by introducing new financial instruments, such as bonds, securitization, venture capital, mutual funds, contractual savings institution and encouraging private sector financial institutions to broaden and diversify their lending portfolio to SME and long-term investment (e.g. infrastructure projects).
- ❖ Recent initiatives taken by GOB and Bangladesh Bank in this regard include: setting up a SME refinance window with support from the ADB and the WB; operating an Equity Entrepreneurship Fund (EEF) to provide equity support to innovative projects in the area of IT and specialized agriculture; facilitating introduction of “factoring” (a form of working capital finance) for SMEs.
- ❖ To facilitate external financing for private investment, BB has come up with proposal to relax conditions for private external borrowing and a guideline has also been prepared for BOI for private borrowing.

However, much more needs to be done. Determined efforts are necessary to meet the challenge with strong support from the policymakers to reaching the PRSP goal of halving the poverty by 2015 based on an accelerated GDP and investment growth.